Supreme Court, U.S.
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No.

In the
Supreme Court of the United States

State of New Jersey, Department of Labor,
Petitioner,

v.

The Reconstituted Committee of Unsecured Creditors
of the United Healthcare System, Inc.,
Respondent.

**On Petition for A Writ of Certiorari to the
United States Court of Appeals
For the Third Circuit**

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

The Federal Unemployment Tax Act (FUTA), 26 U.S.C. § 3301, *et seq.*, imposes an excise tax on employers, based on a percentage of the total wages they pay each year, to meet the costs of providing unemployment compensation for their employees who have lost their jobs. States are required by the FUTA to allow non-profit organizations the option to pay unemployment taxes in advance, or to reimburse the State for unemployment benefits that the State pays to former employees of the organization. *Id.* §§ 3306(c)(8), 3309(a).

The question presented is whether this Court should grant certiorari to resolve the conflict among a growing number of circuits, whether, under this Court's *Anderson-Feiring* test, involuntary reimbursement obligations, imposed upon non-profit employers for the costs of unemployment compensation benefits, constitute excise taxes for purposes of the priority scheme of 11 U.S.C. § 507(a)(8)(E).

LIST OF PARTIES

The only parties to this proceeding are named in the caption. Since the Respondent had instituted this action in the context of the debtor's bankruptcy, the caption in the Court of Appeals lists the debtor, United Healthcare System, Inc. ("United") as well. However, United did not participate in the appeal at any stage.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

LIST OF PARTIES ii

TABLE OF CONTENTS iii

TABLE OF AUTHORITIES v

PETITION FOR WRIT OF CERTIORARI 1

OPINIONS BELOW 1

JURISDICTION 1

STATUTORY PROVISIONS 1

STATEMENT OF THE CASE 2

A. Statutory Background 3

B. Factual Background 4

C. Proceedings Below 5

D. The Court of Appeals Decision 7

REASONS FOR GRANTING THE WRIT 9

I. UNDER THIS COURT'S STANDARDS, THE REIMBURSEMENT OBLIGATIONS OWED HERE WOULD BE HELD TO BE EXCISE TAXES 11

II. THE USE OF ADDITIONAL CRITERIA FOR DECIDING "WHAT IS A TAX" VIOLATES THIS COURT'S RULINGS AND HAS CREATED A CIRCUIT SPLIT 15

III. FAILURE TO REAFFIRM THE CONTINUING VITALITY OF THE *ANDERSON-FEIRING* TEST WILL HAVE SERIOUSLY DETRIMENTAL CONSEQUENCES ON THE STATES 21

IV. THE THIRD CIRCUIT ERRONEOUSLY CONCLUDED THAT THE REIMBURSEMENT METHOD OF FINANCING THE UC FUND WAS NOT AN EXCISE TAX 24

CONCLUSION 27

TABLE OF AUTHORITIES

Page

Cases Cited:

Boston Reg'l Medical Center, Inc. v. Massachusetts Div. of Health Care Finance and Policy,
365 F.3d 51 (1st Cir. 2004) 15, 20-22

Bull v. United States,
295 U.S. 247, 259 (1935) 3

California v. Grace Brethren Church,
457 U.S. 393, 397 (1982) 3, 26

City of New York v. Feiring,
313 U.S. 283 (1941) ..... *passim*

In re Beaman,
9 B.R. 539 (Bankr. D. Or. 1980) 14

In re Boston Reg'l Med. Ctr.,
256 B.R. 212 (Bankr. D. Mass. 2000)
aff'd,
265 B.R, 838 (1st Cir. B.A.P.)
aff'd on other grounds,
291 F.3d 111 (1st Cir. 2002) 14, 20-21

In re Camilli,
94 F.3d 1330 (9th Cir. 1996) 14, 17, 19

In re Carlton Enterprises, Inc.,
103 B.R. 876 (Bankr. N.D. Ohio) (1989) 14

In re Chateaugay Corp.,
177 B.R. 176 (S.D.N.Y. 1995)
aff'd on other grounds,
53 F.3d 478 (2d Cir. 1996) 14

Page

In re Cottage Grove Hosp.,
265 B.R. 241 (Bankr. D.Or. 2001) 13

In re First Truck Lines, Inc.,
48 F.3d 210 (1995),
rev'd sub nom,
U.S. v. Noland,
517 U.S. 535 (1996) 17-18

In re Freymiller Trucking, Inc.,
194 B.R. 914 (Bankr. W.D.Okla. 1996) 16, 20

In re George,
361 F.3d 1157 (9th Cir. 2004) 15, 17, 19

In re Hutchinson,
135 B.R. 890 (Bankr. D.Ariz. 1992) 14

In re Hynes,
229 B.R. 405 (Bankr. W.D. Mich. 1998) 17

In re Lorber Indus. of Ca. Inc.,
675 F.2d 1062 (9th Cir. 1982) ..... *passim*

In re Mid America Co.,
31 F.Supp. 601 (S.D. Ill. 1939) 13

In re Northeastern Ohio General Hosp. Ass'n,
126 B.R. 513 (Bankr. N.D. Ohio 1991) 14

In re Olga Coal Co.,
194 B.R. 741 (Bankr. S.D.N.Y. 1996) 17

In re Pan American Paper Mills,
618 F.2d 159 (1st Cir. 1980) 13

Page

In re Park,
212 B.R. 430 (Bankr. D. Mass. 1997) 17, 19

In re Parkview Hospital-Osteopathic Medical Center,
211 B.R. 603 (Bankr. N.D.Ohio 1996) 14

In re Payne,
27 B.R. 809 (Bankr. D. Kan. 1983) 16

In re Suburban Motor Freight, Inc.,
998 F.2d 338 (6th Cir. 1993) 15

In re Suburban Motor Freight, Inc.,
36 F.3d 484 (6th Cir. 1994) ..... *passim*

In re Tri-Manufacturing & Sales Co.,
82 B.R. 58 (Bankr. S.D. Ohio 1998) 14

In re Voightman,
239 B.R. 380 (8th Cir. BAP 1999) 14, 19

In re Waldo,
186 B.R. 118 (Bankr. D. Mont. 1995)
aff'd
108 F.2d 340 (9th Cir. 1997) 14

In re Wm. Akers, Jr., Co.,
121 F.2d 846 (3d Cir. 1941) 13

National Cable Television Ass'n, Inc. v. United States,
415 U.S. 336 (1974) 8

New Neighborhoods, Inc. v. West Virginia Workers' Comp. Fund,
886 F.2d 714 (4th Cir. 1989) 13, 22

Page

Protective Comm. for Indep. Stockholders of TMT Trailers Ferry, Inc. v. Anderson,
390 U.S. 414, 418 (1968) 24

Raleigh v. Illinois Dept. of Revenue,
530 U.S. 15, 24-25 (2000) 18

Reading Co. v. Brown,
391 U.S. 471, 475 (1968) 24

Sacred Heart Hospital of Norristown v. Pennsylvania Dept. of Labor & Indus.,
209 B.R. 650 (E.D. Pa. 1997) 14, 21

St. Martin Evangelical Lutheran Church v. South Dakota,
451 U.S. 772 (1981) 3, 26

State Indus. Accident Comm'n v. Aebi,
162 P.2d 513 (Ore. 1945) 13

State of New Jersey v. Anderson,
203 U.S. 483 (1906) ..... *passim*

United States v. La Franca,
282 U.S. 568, 572 (1931) 12

United States v. Reorganized CF & I Fabricators of Utah, Inc.,
518 U.S. 213 (1996) ..... *passim*

Worker's Comp. Trust Fund v. Saunders,
234 B.R. 555 (D. Mass. 1999) 16, 19-20

Public Laws Cited:

L. 1971, *c.*346 25

Page

Statutes Cited:

11 U.S.C. §507(a)(1) 2

11 U.S.C. §507(a)(8) 2, 5

11 U.S.C. §507(a)(8)(E) ..... i, 2, 5, 7

11 U.S.C. §507(a)(8)(D) 5, 7

26 U.S.C. §3301 ..... i, 3

26 U.S.C. §3304 ..... 3, 4

26 U.S.C. §3306 ..... i, 4

26 U.S.C. §3309 ..... i, 3, 4

28 U.S.C. §1254(1) 1

N.J.S.A. 43:21-2 4

N.J.S.A. 43:21-3 4

N.J.S.A. 43:21-4 4

N.J.S.A. 43:21-5 4

N.J.S.A. 43:21-7 ..... 4, 5, 8, 25

N.J.S.A. 43:21-7.2 ..... 4, 8

N.J.S.A. 43:21-9 ..... 4, 25

N.J.S.A. 43:21-19 ..... 8, 25

N.J.S.A. 43:21-48 ..... 4, 25

Page

Other Authorities Cited:

Statement Accompanying New Jersey Assembly No. 2501 25

Andrew M. Campbell,
What Claims of Governmental Units Constitute Taxes Qualifying For Priority Under Provisions of § 507(a)(8) of Bankruptcy Code (11 U.S.C.A. §507(a)), 148 *Am. Law. R. Fed.* 351 (2004) 17

PETITION FOR WRIT OF CERTIORARI

The Attorney General of New Jersey, on behalf of the New Jersey Department of Labor, respectfully petitions this Court for a writ of certiorari to review the decision of the United States Court of Appeals for the Third Circuit in this case, and resolve the extremely significant issue presented in this case, which is one that impacts all fifty States.

OPINIONS BELOW

The opinion of the Third Circuit is reported at 396 F.3d 247 (3d Cir. 2005) and reproduced at App.1 . The opinion of the District Court for the District of New Jersey is unreported and reproduced at App.36. The opinion of the Bankruptcy Court for the District of New Jersey is reported at 282 B.R. 330 (Bankr. D.N.J. 2002) and reproduced at App.38.

JURISDICTION

The Court of Appeals entered its judgment on January 24, 2005. There was no petition for rehearing. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

RELEVANT STATUTORY PROVISIONS

1. 11 U.S.C. §507(a) (App. 58)
2. The FUTA, 26 U.S.C. § 3301 (App. 59); §3304 (App. 60); §3306 (App. 62); §3309 (App. 64).
3. N.J.S.A. 43:21-2 (App. 66)
4. N.J.S.A. 43:21-3 (App. 66)
5. N.J.S.A. 43:21-4 (App. 69)
6. N.J.S.A. 43:21-5 (App. 70)

7. N.J.S.A. 43:21-7 (App. 72)
8. N.J.S.A. 43:21-7.2 (App. 79).
9. N.J.S.A. 43:21-9 (App. 86)
10. N.J.S.A. 43:21-19 (App. 91)
11. N.J.S.A. 43:21-48 (App. 95).
12. Statement accompanying New Jersey Assembly No. 2501, *L.* 1971, *c.* 346 (App. 97).

STATEMENT OF THE CASE

After a debtor files a bankruptcy petition under Title 11 of the United States Code (the "Bankruptcy Code" or the "Code"), its assets are divided among its creditors, in accordance with the priority scheme established by the Code. The Code provides for a variety of debts to be given priority in payments, including a first priority for the administrative expenses of the case (such as taxes accruing after the petition is filed). *See* 11 U.S.C. §§ 507(a)(1). App. 58. The eighth priority covers a variety of taxes that accrued prior to the case filing, including excise taxes. *See,* 11 U.S.C. § 507(a)(8). App. 58.

The question presented in this case is whether the involuntary obligation of a non-profit organization to reimburse a State for the unemployment benefits paid by the State to the non-profit's laid-off employees, is an excise tax within the meaning of § 507(a)(8)(E). App. 58-59. The circuits are currently split on how to analyze and answer this question.

The starting point in every case involving application of 11 U.S.C. § 507(a)(8) is whether an exaction by a governmental unit is a tax. However, this fundamental issue – what is a tax – has been decided by lower courts under conflicting and widely divergent standards. Although this Court laid down a broad standard for determining whether an exaction is a tax in *State of New Jersey v. Anderson*, 203 U.S. 483 (1906), *City of New York v. Feiring*, 313 U.S. 283 (1941), and *United States v. Reorganized CF & I Fabricators of Utah, Inc.*, 518 U.S. 213

(1996), lower courts have added a number of additional, and divergent, factors to that test, creating confusion and ensuring a lack of uniformity in this area.

This case presents the Court with a needed opportunity to clarify this important area of the law. Taxes are the "lifeblood of government." *Bull v. United States,* 295 U.S. 247, 259 (1935). It is, therefore, critical for this Court to spell out the standards for determining when payments will be taxes so that all concerned can properly structure their programs so as to protect those vital revenues. Absent such protection, the States' ability to ensure that workers, their families, and business entities will be protected from the hardships caused by involuntary terminations, will be seriously impaired.

A. Statutory Background

New Jersey's Unemployment Compensation ("UC") laws, like those of every State, have been enacted pursuant to the FUTA, 26 U.S.C. §§ 3301-3311. The FUTA, which imposes an excise tax upon employers, is a "cooperative federal-state program of benefits to unemployed workers" to combat "widespread unemployment." *St. Martin Evangelical Lutheran Church v. South Dakota*, 451 U.S. 772, 775, n.3 (1981). A State's UC laws must be federally approved and certified as being in compliance with the federal standards. *Id.* at n.3 (citing to 26 U.S.C. §§3304 and 3309[1]). If certified, "the State is authorized to receive a federal grant to administer the state plan." *California v. Grace Brethren Church*, 457 U.S. 393, 397 (1982).

FUTA requires State UC laws to provide that "all money" paid into the unemployment fund must be credited to the federal Unemployment Trust Fund and "all money withdrawn

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[1] Thus, with every amendment to the FUTA, "States correspondingly have amended their statutes to retain their federal certifications." *St. Martin Evangelical Lutheran Church, supra*, 451 U.S. at 775 n.4.

from the unemployment fund" must be used only to pay UC benefits. 26 U.S.C. §§ 3304(a)(3); (4); 3306. App. 60. FUTA requires nonprofit employers be subject to State UC laws. 26 U.S.C. § 3309(a). App. 64. FUTA however requires that State UC laws allow nonprofits the election to pay their UC liabilities as invoiced, or as quarterly self-assessments at an assigned rate, either of which must be paid "into the State unemployment fund . . ." 26 U.S.C. § 3304(a)(6)(B). App. 61.

New Jersey's UC laws comply with these requirements. Nonprofits must pay UC taxes as self-assessed contributions unless they elect to reimburse the UC fund. *See*, N.J.S.A. 43:21-7.2. App. 79. Monies collected from *all* employers, whether as contributions or reimbursements, are deposited *only* into the UC fund, which can be used *only* to pay UC benefits. N.J.S.A. 43:21-9(a); 21-9(b); 21-9(c). App. 86. The State's UC fund exists for the governmental purpose of providing benefits to unemployed workers. N.J.S.A. 43:21-2 ("economic insecurity due to unemployment is a serious menace to the health, morals, and welfare of the people ... [therefore] a systematic accumulation of funds" for providing unemployment benefits required). App. 66.

UC benefits provided to employees of non-profit entities from the UC fund are identical to those provided to employees of for-profit entities, and such employees are entitled to receive benefits whether or not their employer has made any required payments. N.J.S.A. 43:21-3; 21-4; 21-5. App.66; 69; 70. The reimbursement amount required of non-profit entities fully covers those benefits, but does not include the costs of administration of the fund, additional disability benefits, and amounts to create a solvency reserve. N.J.S.A. 43:21-7(e); 21-48. App.77; 95.

B. Factual Background

United, a non-profit organization, was subject to the State's UC Laws. Prior to its bankruptcy, United elected the reimbursement method of paying its statutory UC liability.

After it filed for bankruptcy on February 19, 1997, United became a contributory employer, paying the unemployment taxes in advance, and having those amounts treated as administrative expenses.

The State filed two proofs of claim in United's case: a pre-petition, priority claim in the amount of $1,156,170.05 and an administrative claim[2] in the amount of $8,302,427.84. The priority proof of claim listed $932,704.37 (exclusive of interest) as reimbursement charges that arose pre-petition, while the administrative proof of claim was comprised of reimbursement charges that arose post-petition totaling $6,240,640.36 (plus interest of $1,982,520.58).[3]

C. Proceedings Below

The Respondent, the Reconstituted Committee of Unsecured Creditors of United Healthcare System, Inc., objected to the State's claims, asserting that reimbursement charges were not taxes entitled to priority status under 11 U.S.C. §507(a)(8), and should be reclassified as a general unsecured claim. The State maintained that its prepetition claim merited priority status under 11 U.S.C. §507(a)(8)(D) or (E), and that its postpetition claim was entitled to be treated as a first-priority administrative expense.

The Bankruptcy Court's extensive opinion agreed with the State's position that its claims were entitled to priority as an excise tax under 11 U.S.C. §507(a)(8)(E). App. 38. The court

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[2] These payments were made post-petition but were based upon pre-petition employment and wages paid to United's employees , and thus, before United returned to being a contributory employer.

[3] The claims also included unpaid employer State disability plan contributions and assessments, and worker unemployment and disability contributions, payable pursuant to N.J.S.A. 43:21-7(e) and N.J.S.A. 43:21-7(d)(1)(E). These liabilities are imposed upon all employers, including nonprofit employers who elect to make payments in lieu of contributions.

noted that both the FUTA and its legislative history "are simply silent as to how to characterize the payments in lieu of contributions" (App. 51) and that "[a]pplication" of the Supreme Court's broad definition of a tax set forth in *Feiring*, *supra*, and *Anderson*, *supra*, was not "an easy task ... in the bankruptcy context." App. 44. The use of additional limiting criteria by lower courts such as *In re Lorber Indus. of California, Inc.*, 675 F.2d 1062 (9th Cir. 1982) ("*Lorber*"), and *In re Suburban Motor Freight, Inc.*, 36 F.3d 484 (6th Cir. 1994) ("*Suburban II*")) had made the issue more complex and uncertain.

After examining all the relevant State statutory UC provisions in this regard, the Bankruptcy Court ruled that (i) the exactions in the form of reimbursements were "an involuntary pecuniary burden imposed by the legislature," since United, like any other employer, was obligated by State statutes to finance and make payments into the State's UC fund, and thus, "was only able to choose how to make the payments, not whether to make the payments;" (ii) New Jersey UC laws were enacted purely "for a public purpose and pursuant to the police power" of the State, and (iii) that the reimbursement scheme met even the added limitations imposed by *Suburban II*, *supra*, in that the exactions were "universally applicable" and no private creditors with like claims were disadvantaged.[4] App. 47, 48.

The court further held there was no "material difference" between contributions and payments in lieu of contributions, and that both went into the UC fund to pay "benefits designed to prevent unemployed workers from becoming a public burden." App. 48-49. Congress had not intended to exempt

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[4] The court found that the State's ability to secure a surety bond from an electing employer, while not necessarily a non-tax attribute, may be viewed to violate the additional requirement in *Suburban II*, *supra*, that a surety with an identical claim should not be disadvantaged. App. 53. Even so, the court held, this "single non-tax characteristic" would not suffice to deny the reimbursement scheme as being a tax. *Ibid.*

nonprofits from payment of "state unemployment taxes," but only to "a reduced tax burden." App. 51. The court concluded that the reimbursements were excise taxes, because "like contributions [they] arise from the privilege or act of employing workers." App. 54. Thus, the State's claims were entitled to priority under Section 507(a)(8)(E).[5] *Ibid.* The District Court affirmed in all respects. App.36.

D. The Court of Appeals Decision

In a 2-1 opinion, the Third Circuit reversed. App.1. The majority noted that this Court's decisions dealing with the question of "what is a tax"– *Anderson, supra,* and *Feiring, supra* – were not dispositive because they were decided under the Bankruptcy Act, which purportedly provided a broader priority treatment of "government obligations" than under the Code's current tax priorities. App. 9. Accordingly, it sought to apply the "functional" analysis in *CF & I* (which had been used to determine whether a payment was a tax or a penalty) to aid it in determining whether the reimbursement was a "tax" or some other form of "government obligation." App.14-15.

The majority acknowledged the case as a "close one" since "reimbursement payments and quarterly contributions are complementary." App. 19. The court concluded, however, that because the reimbursements are "direct[ly] correlat[ed]" to the payments made by the State to the laid-off employees, they were "an alternative to paying taxes rather than ... an alternative method" of paying taxes. *Ibid.* The FUTA was "germane" only insofar as it mandated States to provide the choice of payment, but did not decide "the question surrounding the nature of this obligation." App. 23.

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[5] The court held that the postpetition portion of the taxes would not be given first-priority administrative status, because they were based on pre-petition employment. App. 56. The State did not appeal the administrative status determination. The court also ruled against the State's alternative argument that the claims were entitled to priority status under Section 507(a)(8)(D), App. 54, and the State did not appeal that issue.

The majority held that the contributions and reimbursements were distinct obligations because they were stated in separate sections of the statute, N.J.S.A. 43:21-7 and N.J.S.A. 43:21-7.2 respectively, and were defined separately in one section of another statute, N.J.S.A. 43:21-19(f).[6] App. 20. It further held that the reimbursements "do not raise funds to support a general government undertaking," unlike contributions, because the payments "only reimburse" the State for specific payments it has made. App. 21. Thus, while reimbursement payments are "intermingled in the same state fund" with all other contributions, they are "more like a promise [by the non-profit employer to pay] in exchange for the privilege of employing individuals in the state without being required to pay state [UC] obligations." App. 22.

The statutory scheme, according to the majority, created a contract between the State and a non-profit employer by which "[t]he state will allow" such an employer "to conduct business without" contributing to the state UC fund, and in exchange, "the state will pay the [UC] benefits" to the employees. *Ibid.* This relationship, the court held, resulted in "a debt." *Ibid.* This alleged debt was akin to a fee (as in *National Cable Television Ass'n, Inc. v. United States*, 415 U.S. 336 (1974)), because the State purportedly bestowed a benefit on non-profit employers not available to other employers, namely, the option of funding the UC costs on a reimbursement basis. App. 23.

Chief Judge Scirica dissented. While viewing this as a "difficult and close case," in light of the clear public purpose of the UC laws and the involuntary nature of the exactions (since the electing employer could not "evade its responsibility to the [UC] fund altogether"), he concluded that the reimbursements "more closely resemble a tax than other kinds of government assessments, fees in exchange for benefits, or penalties." App.

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[6] N.J.S.A. 43:21-19(f) defines "contributions" as "money payments to the State Unemployment Compensation Fund." The same sub-section defines "payments in lieu of contributions" as "money payments to the State Unemployment Compensation Fund" made by electing employers. App.91.

24-31. Any distinction between the contribution and reimbursement methods of funding the State's UC fund was more of "degree rather than kind." App. 24.

The Chief Judge reasoned that the "statutory purpose of the obligation is to benefit the former employees and the public good, not the employer." App. 28. The reimbursements method of payment did "not grant an affirmative benefit on the non-profit employer." App. 28-29. The debtor was not given a benefit of being allowed to operate in the State without making contributions to the UC fund. Like all other employers, it was saddled with an involuntary burden to "support the [UC] fund" *albeit* allowed to use a different means to satisfy the obligation. App. 29. The dissent concluded that the reimbursements qualified as a priority excise tax. App. 31.

REASONS FOR GRANTING THE WRIT

This case cries out for review by this Court. The issue significantly and adversely affects the taxing powers of the State and the proper administration and funding of the State's UC funds. The issue equally impacts all fifty states with respect to their right to tax nonprofit employers operating within their borders, and exact such tax as reimbursements.

The fundamental question of "what is a tax?" and what standard shall be used to judge that question, arises not just in unemployment compensation but in many other, equally critical areas. It has, for example, confounded the courts in the context of state Workers Compensation (WC) programs. Those programs use a wide variety of means to initially fund the costs of the program (including direct premium payments to the states as the sole provider of benefits, payments to the state as an alternative to private insurance coverage, or self-insurance by the employer). Virtually all states also pay benefits to workers whose employers have failed to obtain insurance or can no longer afford to satisfy their self-insurance obligations and

impose reimbursement obligations on those employers, akin to those imposed on the non-profit entities here.

The courts, however, have struggled in recent years with how to determine whether the reimbursement obligations are taxes and entitled to priority treatment. When courts relied only on the *Anderson-Feiring* test enunciated by this Court, they had relatively little difficulty in completing the analysis with respect to any of these benefit payments. However, a number of courts – most notably the Sixth Circuit – devised new tests to determine when a government payment is a tax for priority purposes. Since the addition of those new factors, there has been a rising chorus of complaint from the courts about the purported difficulty of applying the original *Anderson-Feiring* test. Moreover, in marked contrast to the largely uniform treatment of all of these payments as taxes in earlier years, many recent decisions have denied that treatment to one or more of these types of obligations. It is as to those accretions onto this Court's holding, and their devastating effect on the availability of funding for employee benefits, that the State seeks review.

In particular, in this case, by converting a FUTA-mandated alternative method of collecting tax obligations into a contract between the State and electing non-profit employers, the Third Circuit's decision has subverted the express intent of the FUTA to allow States to impose UC taxes on every nonprofit employer. With the ever-increasing number of bankruptcy filings by non-profit entities in recent years, which almost inevitably will result in layoffs, the States' UC fund will incur substantial costs to provide benefits to the employees of those entities. If those funds are not collected from the non-profit employer in question, the result will be to force higher premiums to be assessed against other employers, thus impairing their operations, and possible jeopardizing continued payments. The result would imperil the solvency of the very funds established to protect employees who have lost their jobs through no fault of their own.

It is, therefore, critical for this Court to spell out clearly what are the standards for determining when payments will be taxes so that all concerned can properly structure their programs so as to protect those vital revenues. The impact of this issue, nation-wide requires review by this Court. Determination of the universally applicable and proper standard will help the courts in resolving these oft-occurring issues, not only for UC reimbursements, but also as to a wide variety of payments.

I. UNDER THIS COURT'S STANDARDS, THE REIMBURSEMENT OBLIGATIONS OWED HERE WOULD BE HELD TO BE EXCISE TAXES.

In determining whether a state exaction is an "excise tax," the first issue that the Court must determine is whether the payment is a tax at all. Almost a hundred years ago, this Court stated the parameters for that judgment for the purpose of applying priorities in a bankruptcy case. "Generally speaking, a tax is a pecuniary burden laid upon individuals or property for the purpose of supporting the government . . . " and "capable of being enforced by action against the will of the taxpayer." *Anderson*, *supra*, 203 U.S. at 492. While a debt is an "obligation for the payment of money founded upon contract, express or implied" a tax is "levied for the support of the government or for some special purpose authorized by it" without a "taxpayer's consent." *Ibid.*

This Court reiterated those parameters 35 years later in the *Feiring* case, stating that "the [bankruptcy] priority . . . extends to those pecuniary burdens laid upon individuals or their property, regardless of their consent, for the purpose of defraying the expenses of the government or of undertakings authorized by it." *Feiring*, *supra*, 313 U.S. at 285. While the measure was in the form of a sales tax, it was enacted as "an emergency revenue measure to defray the expense of unemployment relief." The Court held that the levy was a tax, because a "pecuniary burden so laid upon the bankrupt . . . for the support of the government, and without his consent thus has all the characteristics of a tax entitled to priority of payment in

bankruptcy." *Id.* at 287. Thus, while "an ordinary debt due the state is not entitled to priority," a "demand . . . for a tax, the unqualified duty to pay which was placed by the statute on the seller" is so entitled. *Id.* at 288.

Fifty-five years later, in 1996, the Court reaffirmed the time-tested *Anderson-Feiring* standard in the case of *CF&I Fabricators, supra,* stating that "[a] tax is an enforced contribution to provide for the support of government; a penalty . . . is an exaction imposed by statute as punishment for an unlawful act.'" 518 U.S. at 224 (quoting *United States v. La Franca*, 282 U.S. 568, 572 (1931)). The Court noted that despite the passage of time, and amendments to the Bankruptcy Code with respect to treatment of taxes in bankruptcy, Congress had never rejected its statement of the tests in *Anderson, supra*, and *Feiring, supra,* or tried to create a different test. *CF&I Fabricators, supra*, 518 U.S. at 224.

During that time period, the Ninth Circuit restated the *Anderson-Feiring* test in *Lorber, supra*, 675 F.2d at 1066, and held that an exaction was a tax if it was (i) an involuntary pecuniary burden, (ii) legislatively imposed; (iii) under the police or taxing power of the state; and (iv) for public purposes, including the purposes of defraying expenses of government or undertakings authorized by it. While somewhat more elaborate than this Court's version of the test, *Lorber* appears to add nothing of substance, so that cases analyzed under that test are equally applicable here.[7]

In applying the pure *Anderson-Feiring* (and *Lorber)* test to all three types of payments (UC reimbursements, WC reimbursements, or WC premium payments), courts initially had little trouble in concluding that the payments were "taxes"

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[7] The issue in *Lorber* turned on how to decide whether a payment owed to the state was being made"voluntarily" so as to constitute a fee, or whether it was an involuntary payment so as to constitute a tax. That inquiry is equally relevant under this Court's test.

for purposes of bankruptcy priorities.[8] In *In re Pan American Paper Mills*, 618 F.2d 159, 162 (1st Cir.1980), for instance, the First Circuit held that WC premiums, like UC contributions, were entitled to the "tax" priority under Section 64(a)(4) of the Bankruptcy Act, noting that the "pertinent questions about a so-called premium are whether the government compelled the employer to pay the exaction and whether the payment was for a public purpose." Similarly, in *State Indus. Acc. Com'n v. Aebi*, 162 P.2d 513 (Or. 1945), the court found that WC premiums, like UC contributions, were required payments made for a public purpose, even though the employer had the ability to opt out of the WC system entirely (and remain exposed to tort liability). Moreover, the court rejected the notion that the payments were any less a tax because the law did not equally protect "an insurance carrier claiming unpaid insurance premiums from a bankrupt. This is not an inconsistency. It is merely an example of the distinction between the sovereign power of the state and the rights of private citizenry." *Id.* at 371.

The Fourth Circuit explicitly adopted that view in *New Neighborhoods, Inc. v. West Virginia Workmen's Comp. Ins. Funds*, 886 F.2d 714 (4th Cir. 1980), where it concluded that WC premiums were taxes, and that it was irrelevant that the same priority might not accrue to a private WC insurer (quoting from *Aebi, supra*).

Cases applying the *Anderson-Feiring-Lorber* test to find that UC reimbursements were excise taxes include *In re Cottage Grove Hosp.*, 265 B.R. 241, 247 (Bankr. D. Ore. 2001) ("[n]o sound public policy" to distinguish UC and WC

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[8] Because of the universal obligation on for-profit employers to make unemployment contributions, the fact that the state is the single payor of unemployment benefits to employees, there has been little or no dispute that contributions owed by employers (either for-profit or non-electing tax exempt employers) are excise taxes. *See, e.g., In re Wm. Akers, Jr., Co.*, 121 F.2d 846 (3d Cir. 1941); *In re Mid America Co.*, 31 F.Supp. 601 (S.D.Ill. 1939). United itself is one such example. App. 41.

reimbursements); *In re Parkview Hospital-Osteopathic Medical Center*, 211 B.R. 603, 612 (Bankr. N.D. Ohio, 1996); (not "patently unreasonable" to deem reimbursables a tax). *See, also, In re Sacred Heart Hosp. of Norristown*, 209 B.R. 650 (E.D.Pa. 1997) and *In re Boston Regional Medical Center*, 256 B.R. 212 (Bankr. D. Mass. 2000), *aff'd*, 265 B.R. 838 (1st Cir. B.A.P. 2001) – both of which found the payments to be taxes, and both of which were overruled – *Sacred Heart* by the decision at issue here, and *Boston Regional* by *In re Boston Regional Medical Center, Inc. ("Boston Regional I")*, 291 F.3d 111 (1st Cir. 2001) *Cf., In re Northeastern Ohio General Hosp. Ass'n*, 126 B.R. 513, 515 (Bankr. N.D. Oh. 1991) ("undisputed" that UC reimbursements are a tax).

In the WC area, cases using the *Anderson-Feiring-Lorber* test to deem the exactions a tax, include *In re Camilli*, 94 F.3d 1330, 1333 (9th Cir. 1996), *cert. denied*, 519 U.S. 1113 (1997) (reimbursement obligations "part of a complex system designed . . . to provide universal availability of workers' compensation benefits to employees in the state;" obligation was "the product of legislative fiat; . . . wholly beyond the control of the debtor"); *In re Voightman*, 239 B.R. 380 (8th Cir. BAP 1999) (premiums); *In re Waldo*, 186 B.R. 118, 125 (Bankr. D. Mont. 1995) (reimbursement) *aff'd*, 108 F.2d 340 (9th Cir. 1997); *In re Chateaugay Corp.*, 177 B.R 176, 184 (S.D.N.Y. 1995), *aff'd on other grounds*, 89 F.3d 942 (2d Cir. 1996) (premiums); *In re Hutchinson*, 135 B.R. 890 (Bankr. D.Az. 1992) (premiums); *In re Tri-Manufacturing and Sales Co.*, 82 B.R. 58 (Bankr. S.D. Ohio 1988) (premiums); *In re Beaman*, 9 B.R. 539 (Bankr. D.Ore. 1980) (reimbursements). *But, see, In re Carlton Enterprises, Inc.*, 103 B.R. 876 (Bankr. N.D. Ohio) (1989) (reimbursements not excise tax).

Had this Court's test been the only standard used, there is little doubt that the State's UC reimbursement claim, as in the numerous cases cited above, would have been found to be an excise tax. The claim arose from a mandatory obligation, imposed on the employer by statute, to comply with one of two alternative means of satisfying its duty to provide for its laid-off

employees. The State law explicitly provides that such benefits are provided for the public good, N.J.S.A. 43:21-2, (App. 66) and the courts have universally concluded that the unemployment compensation system are for an appropriate governmental purpose and an undertaking for the common welfare. As such, it was plainly a tax. The only remaining issue is whether it is an "excise" tax, an issue as to which courts generally have had no difficulty in finding for the government.[9] Absent the confusion engendered by the recent line of cases, it is unlikely that any court would have required any further analysis.

II. THE USE OF ADDITIONAL CRITERIA FOR DECIDING "WHAT IS A TAX" VIOLATES THIS COURT'S RULINGS AND HAS CREATED A CIRCUIT SPLIT

Rather than applying this Court's existing, straightforward analytical standard, the court here concluded that it was required to engage in a far more searching analysis and to review an entire series of factors to make a "functional analysis" of whether this payment was a tax, or some sort of contractual debt. App. 19-24. That analysis, in turn, arose out of a series of cases in which "lower courts have . . . struggled in applying the *Feiring-Anderson* analysis" in bankruptcy cases. *In re Boston Regional Medical Center,* 365 F.3d 51, 58 (1st Cir. 2004) (*"Boston Regional II"*).

In particular, in *In re Suburban Motor Freight, Inc.*, 998 F.2d 338, 341 (6th Cir. 1993) (*"Suburban I"*) (dealing with WC premiums), the Sixth Circuit expressed strong concerns about

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[9] Note that in *Suburban II,* the Sixth Circuit agreed that if the reimbursements were a tax, they would be an excise tax as being "indirectly assessed ... on [the] 'transaction or act of employing.'" *Id.*, 36 F.3d at 488, n.2. The cases noted above also concluded that the UC and WC payments were "excise" taxes. *But, see, In re George*, 361 F.3d 1157 (9th Cir. 2004), denying excise tax status to WC reimbursements because they were not imposed on a "transaction," but on the failure to obtain insurance.

whether application of the *Anderson-Feiring* test was too generous and stated that "overemphasis on the 'public purpose' element would eliminate all distinction between 'taxes' and 'fees' or other money owed the Government, enabling the State to prevail consistently against private creditors with arguably equal claims." *Id.* at 341. It noted that "[t]his Circuit has stood nearly alone in expressing this concern." *Ibid.*

A year later, in *Suburban II*, *supra*, where the State sought to also be reimbursed for the actual benefits it paid to the debtor's employees, the Sixth Circuit returned to the concerns that it had expressed in *Suburban I*, about the assertedly overly generous standard created by the *Anderson-Feiring* test. Therefore, the *Suburban II* court concluded that two additional requirements must be added to the *Lorber* test so as properly to distinguish taxes from fees or other payments to the government. The court must find that a governmental exaction is (i) "universally applicable to similarly situated entities; and (ii) that according priority treatment to the government claim [will] not disadvantage private creditors with like claims." *Id.*, 36 F.3d at 488-89. Under this new test, it concluded that the reimbursement obligation was *not* a tax.

Since that decision, the Sixth Circuit no longer stands alone. To the contrary, its new test has gained numerous adherents, and led many courts to conclude that they must engage in detailed examinations of the minutiae of state payment obligations to determine if they resemble claims owed to any other party, or if they lack some degree of universal coverage. *See, e.g., In re Payne,* 27 B.R. 809 (Bankr. D. Kan. 1983) (reimbursement of workers benefits paid by State not a tax because the of the predominant non-tax characteristics such as, remedies available to the worker against the employer, no automatic statutory lien in favor of State, and State's status more as a subrogee); *In re Freymiller Trucking, Inc.*, 194 B.R. 914 (Bankr. W.D. Okla. 1996) (reimbursements not a tax because under *Anderson*, *supra*, they were not assessed at a fixed rate, and were akin to a subrogation claim); *Worker's Compensation Trust Fund v. Saunders*, 234 B.R. 555 (D. Mass.

1999) (*Anderson-Feiring* test ignores the "critical question" of whether granting "priority status to a governmental claim meets the purposes and policy" of the Bankruptcy Code); *In re Park*, 212 B.R. 430 (Bankr. D. Mass. 1997). *See, generally*, Andrew M. Campbell, *What Claims of Governmental Units Constitute Taxes Qualifying For Priority Under Provisions of § 507(a)(8) of Bankruptcy Code (11 U.S.C.A. §507(a))*, 148 *Am. Law. R. Fed.* 351 (2004). In the process, rather than providing greater clarity, it have only spawned more confusion.[10]

In suggesting, moreover, that the limitations were needed because the *Anderson-Feiring* test was purportedly not well-suited to bankruptcy issues, those cases ignore the fact that both *Anderson* and *Feiring were* bankruptcy cases and analyzed precisely the same priority issues courts face now. Thus, the continued reluctance of many lower courts to apply this Court's test, without added embellishments and limitations, simply cannot be justified by a purported need to deal with "new" issues that had not confronted this Court.

Instead, the use of added tests to "protect" creditors from what is viewed as an overly generous test, appears to be more akin to the reasoning used by the Sixth Circuit in *In re First Truck Lines, Inc.*, 48 F.3d 210 (1995), where it relied on its view of appropriate bankruptcy policy considerations as a reason to override the Code's grant of administrative status to postpetition tax penalties. The Court overruled that decision in *U.S. v. Noland*, 517 U.S. 535 (1996) holding that courts could not take upon themselves the power to make a "categorical determination" that such penalties did not warrant priority status in order to further the goals of the Code. This Court

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[10] Ironically, while *Suburban II* found the WC reimbursements were *not* taxes, virtually all other courts considering the issue under the *Suburban II* test *have* found them to be taxes. *See, e.g., Camilli, supra,; In re Hynes*, 229 B.R. 405 (Bankr. W.D. Mi. 1998)*; In re Olga Coal Co.*, 194 B.R. 741 (Bankr. S.D.N.Y. 1996). *But, see, George, supra.* This contradiction suggests that the Sixth Circuit was simply using the tax issue to address other concerns it had with the State's claim.

reiterated that principle in *Raleigh v. Illinois Dept. of Revenue*, 530 U.S. 15, 24-25 (2000) noting that "[b]ankruptcy courts are not authorized in the name of equity to make wholesale substitution of underlying law controlling the validity of creditors' entitlements, but are limited to what the Bankruptcy Code itself provides." In doing so, it similarly rejected the lower court's attempt to impose a new, bankruptcy-specific standard for proving tax claims, merely in order to satisfy a perceived need to improve on the statute, as written.

The decision below similarly evinces a view that the courts must invent a more searching test in order to satisfy the goals of the bankruptcy system, asserting that the *Anderson-Feiring* test must be updated because the scope of priority "government obligations" had changed since the Bankruptcy Act was replaced by the Code App. 9, 14. That statement though, ignored the fact that the priority provisions of both the Act and the Code that the Court addressed in its *Anderson-Feiring* test dealt explicitly with "taxes," not some amorphous and changing category of "obligations." While the Act gave priority to *all* taxes, and the Code gives priority to only *some* taxes, nothing in that limitation suggests any reason to use a different test to determine the basic question of what *is* a tax. Indeed, this Court expressly reiterated its basic test as recently as 1996 in *CF & I, supra*. There also, this Court rejected a bankruptcy court's equitable subordination of a government penalty claim because of the lower court's justification that governmental claims should be downgraded to better serve the needs of other creditors in the case. *Id.*, 518 U.S. at 227-28.

Despite the repeated endorsement by this Court of its broad *Anderson-Feiring* test, and its other cases rejecting efforts by lower courts to strain the language of the Code dealing with the priorities for government claims, the decisions since *Suburban II* have increasingly moved away from applying that test on its own terms. In doing so, though, the use of *Suburban II's* new requirements has caused much difficulty for the courts and led some to rely on a plethora of factors to deny tax status to state claims.

The search for similar creditors in the case who might be disadvantaged by granting tax status to the State's claim, for instance, has been applied even if the absence of any actual creditor. In *George*, *supra*, for example, the Ninth Circuit held that "if a creditor similarly situated to the government can be *hypothesized* under the relevant statute, then [even] by the reasoning of *Camilli*, the government claim is not a tax." *Id.* at 1162 (emphasis added) (thus, disavowing its own prior decision that WC reimbursements are a tax in *Camilli*). Simply because there *might* be another employer that *might* have a separate obligation to pay benefits to an uninsured employee with a cumulative injury, which employer's contribution claim against the debtor *might* compete with the State's reimbursement claim, so that the employer *might* be disadvantaged if the State's claim were treated as a tax. That string of possibilities, the Ninth Circuit held, was enough to deny tax status to the State's claim.

Indeed, *Suburban II* gives no clear basis for how to define which entities are "similarly situated,." thus generating new bases for debtors to challenge state claims[11] Nor does it explain how its new requirement squares with the principle that taxes need not be applied to all entities, but may be restricted to certain classes of employers. Similarly, the determination of which private entities have "like" claims, nor when a requirement is "universally imposed," has not been easy.[12]

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[11] In *Voightman*, *supra*, for example, the debtor unsuccessfully challenged the WC premiums because the system did not apply to farmer-employers, which it claimed were similarly situated to other business employers.

[12] In *In re Park*, *supra*, for instance, the court denied tax status to the state's WC reimbursement claim because the state law only required such payments to be made by uninsured employers who had injured employees who were paid from the Fund. 240 B.R. at 436. The fact that such employers were the only ones who *could* engender a liability to the state, and who, therefore, could incur such a tax debt, was apparently irrelevant in the court's view. In *Saunders, supra*, on the other hand, the court held that a state's reimbursement scheme was not universally applied

The lower courts' struggle to interpret and apply the various proposed tests has been noted by a variety of courts. *See, e.g., Boston Regional I*, 291 F.3d at 121; *In re Park*, *supra*, 212 B.R. at 435-36 (observing the profusion of cases and standards); *Saunders*, *supra*, 234 B.R. at 562-564. The result has led to courts to look to a profusion of inconsistent factors, although rarely with any agreement on their significance, none of which are dictated by this Court's test, to decide whether a payment is a tax. In *Boston Regional I*, for instance, the court observed that the current morass of decisions could "arguably" make UC reimbursements a tax, but the analysis was "flexible enough" to deny tax status to the obligations. *Id.* at 121-22. The court placed great weight, though, on the fact that non-profit employers were not charged for the fund's "administrative costs, additional benefits, or the solvency margin" and that the government could have, but did not procure a surety bond, finding that the latter factor "tip[ped] the scales" in favor of the payment not being a tax. *Ibid. See, also*, *In re Freymiller Trucking*, *supra*, 194 B.R. at 917 , where the court relied on the fact that reimbursements were not assessed at a fixed rate, and thus, not a tax, although nothing in this Court's test imposes that requirement.

The First Circuit after determining that UC reimbursements were not taxes, revisited the priority tax issue with respect to assessments imposed on all health care facilities in the state to create the Uncompensated Care Pool that reimbursed facilities with a disproportionate amount of uncompensated care for indigent patients. The court concluded that the fund payments *were* taxes and "fit[] sufficiently within the broad definition of an excise" tax, although the assessments were not uniformly imposed at the same rate, and although the assessments were a condition to maintaining a license. *Boston Regional II*, 365 F.3d at 55, n.3, 64-65. In so concluding, it again noted that the

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merely because it stated that the state "may" seek reimbursement from a non-profit employer, but not that it "shall" do so. 234 B.R. at 565.

conflicting opinions in this area made its task a "struggle."*Id.* at 58.

In the present case, the Third Circuit disagreed with the reasons the First Circuit relied upon in *Boston Regional I* to find that the UC reimbursements were not a tax, and specifically rejected the First Circuit's view that the availability of a bond weighed against tax status. App. 19-20. Nevertheless, the court reached the same result by its "functional approach," after agreeing with the views expressed in *Suburban II*. In doing so, it overruled the decision in the *Sacred Heart, supra*, which had found such payments to be taxes based on a straightforward application of the *Anderson-Feiring-Lorber* test. App. 20.

As the cases discussed above demonstrate, and as pointed out over and over again by the circuit courts, the general issue of what standard to use to decide "what is a tax," and the particular issue of whether UC reimbursements are taxes, have continued to confound the courts. The cases have had varying results in recent years, with some courts applying the *Anderson-Feiring-Lorber* test, while other courts have held that they must also give a "particular and separate weight to the Bankruptcy Code's principle of equal distribution of the debtor's estate," the factor which led to the Sixth Circuit's introduction of additional, limiting factors in *Suburban II*. *See, Boston Regional II*, 365 F.3d at 58. In light of these conflicting standards and decisions, it becomes ever more difficult for legislatures to determine what *is* a tax, and how to structure revenue requirements so as to ensure that amounts owed to the government *will* be treated as taxes.

III. FAILURE TO REAFFIRM THE CONTINUING VITALITY OF THE *ANDERSON-FEIRING* TEST WILL HAVE SERIOUSLY DETRIMENTAL CONSEQUENCES ON THE STATES

These cases have thus left the certainty of the reimbursement method of financing a fund in a state of flux.

Only this Court can bring a proper and final resolution to this crucial and significant issue that impacts all fifty States. The States are forced by federal law to offer non-profit employers the right to use the reimbursement method of payment of their share of the UC costs, to support the government's undertaking to provide UC benefits to unemployed individuals, as a means to survive during their period of unemployment.

The opinion at issue here, and that of the First Circuit in the unemployment context, directly undermine this federal-state co-operative effort. By arbitrarily transforming a required reimbursement tax into a fee or a contractual debt, the decisions greatly diminish government's ability to further the public policy goal of paying benefits to *all* unemployed workers. Similar decisions in the workers' compensation area equally undercut the government's ability to ensure that *all* workers injured or made ill in their employer's service receive benefits, without unduly burdening the State or other employers within the State.

The opinion of the court of appeals has shaken the very integrity and solvency of the States' UC fund, a fund held in trust for payment of unemployment benefits. As aptly stated by the Fourth Circuit, denying priority status to a state's claim would enhance the share of the general unsecured creditors, who might be seen as the "'little fellows' [b]ut so are the injured employees who depend upon the financial soundness of the Fund and are thus indirectly benefitted by priority status in bankruptcy." *New Neighborhoods, supra* 886 F.2d at 719. *See, also, Boston Regional II*, 365 F.3d at 65 (even if loss due to reclassification of State's claim is passed on to other non-debtor hospitals, State still loses because the hospitals are "instruments of the government's intended services to indigents: losses to them impact adversely the public program").

Those concerns apply with considerable and equal force here. The State's loss will, in the end, also be visited upon its citizens and businesses. If the State cannot recover the amounts

unpaid by nonprofit debtors that have elected reimbursement status, it will be forced to increase the tax paid by financially responsible employers to maintain the UC fund and adhere to the permeating public purpose of maintaining such fund. The burden of covering unpaid bankruptcy losses should not be borne by all other financially responsible employers, when such additional tax liability could jeopardize *their* economic stability and ability to maintain their own work forces.

Alternatively, or additionally, the State could be forced to seek surety bonds from non-profit entities for the full amount of their potential unfunded liabilities. Those amounts, as shown here, could be enormous, if they are set at an amounts high enough to fully protect the UC fund from the severe depletion resulting from the loss of tax status.[13] Bankruptcies of non-profit employers have become more prevalent and each such case could implicate this issue. If the State cannot be protected during the claims process, it will be obligated to impose higher burdens on *all* such employers in order to avoid future problems. As pointed out by the dissent in this case, relegating the reimbursement payments to a general unsecured status "will likely increase the non-profit employers' operating costs" if the State would be forced to seek surety bonds in the future. App. 30. The absence of a mandated bond reduces the "costs to the non-profit employers of doing business in New Jersey" as does permitting them to finance the UC fund on a reimbursement basis. *Ibid.* The majority's ruling would force the State to"require a bond" from the reimbursable employers, defeating FUTA's purpose of "minimiz[ing] the cost of non-profit organizations' participation in the [UC] scheme." *Ibid.*

Moreover, even if legislatures attempt to restructure their revenue programs to satisfy these new standards, the confusion and ambiguities noted above will continue to confound their efforts and limit their ability to appropriately tailor their use of

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[13] Here, for instance, the State could lose as much as $8 million of its $9.5 million in claims if its reimbursement obligation is treated as a general unsecured claim instead of a tax obligation.

their taxing powers. The creative use of the "fee" concept by the Third Circuit's decision herein, to avoid treatment of the State's claim as a tax, shows the issues that can be created even with respect to legislation that was plainly designed to impose a universal revenue obligation. Such problems are neither inherent in the Code, nor required by this Court's prior decisions. They arise solely from the failure of some courts below to follow this Court's prior guidance.

. The difficulties for States that are engendered by the new tests will continue until this Court returns to the issues that it thought had been put to rest in *Feiring* and provides additional guidance to the lower courts on how to determine which involuntary state exactions truly are taxes. Accordingly, this case should be reviewed and resolved in all respects by this Court. The public interest is best served by immediate determination of this important federal issue so that state officials are not forced to implement remedies to protect the integrity of the UC fund that may adversely affect the very employers purportedly being protected by these provisions. *See, Reading Co. v. Brown*, 391 U.S. 471, 475 (1968) (certiorari granted "because the issue is important in the administration of bankruptcy laws and is one of first impression in this Court"); *Protective Comm. for Indep. Stockholders of TMT Trailers Ferry, Inc. v. Anderson*, 390 U.S. 414, 418 (1968) (certiorari granted as case "present[ed] important questions under the bankruptcy laws"). Each of the fifty States will be impacted by the resolution of this federal question, therefore, this Court's review is of crucial and vital significance.

IV. THE THIRD CIRCUIT ERRONEOUSLY CONCLUDED THAT FINANCING OF THE UC FUND BY REIMBURSEMENTS WAS NOT A TAX.

Certiorari is also warranted because the decision below is plainly wrong. The majority opinion of the Third Circuit, informed by the added complexities it erroneously viewed as being required under *Suburban II*, erred in concluding that the

reimbursement method of payment does not support the costs of a government undertaking. The court's hyper-technical reliance on mere historical quirks of drafting ignores the overall structure of the funding obligations.[14] Both obligations are defined identically to mean "payments made into the UC Fund." N.J.S.A. 43:21-19(f). Both obligations go into the same fund. N.J.S.A. 43:21-9(a). The money in the fund is used to pay the same amount of unemployment benefits for the employees of *all* employers.[15] *All* employers must make the payments they are liable for from their own funds and cannot deduct any sums from their employees' salaries. N.J.S.A. 43:21-7.2 (d); 43:21-7(a)(1). Costs and assessments to maintain the UC Fund are imposed upon *all* employers, including electing non-profit employers. N.J.S.A. 43:21-48.

Second, the court's conclusion that reimbursements were "a promise in exchange for the privilege of employing" persons within the state (App. 22) is incorrect. The relationship between the States and the non-profit employer is not one of voluntary, arms-length contractual partners. Indeed, States have no choice about whether to operate a UC system for the benefit of their citizens and the economy as a whole. In operating that system, they have no choice about whether to allow the reimbursement option to the non-profit. The non-profit employer has no choice about being required to pay for the cost of UC benefits for any persons that it employs within the State or any ability to negotiate for a lesser amount of benefits to be afforded to its employees in return for a lesser amount of payments to the states. The ability of the non-profit to opt to take advantage of a less costly option for satisfying its obligation to its employees does not make the exaction a type of voluntary fee. To suggest

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[14] The reimbursement obligation is included in a separate section simply because it was added in 1971 after Congress changed the federal FUTA in 1970 to cover non-profit employers, and allow States to tax them, *albeit* by use of the alternative means of payments. *See*, Statement accompanying Assembly No. 2501, *L.* 1971, *c.* 346. (App.112).

[15] N.J.S.A. 43:21-9(b); (c); N.J.S.A. 43:21-7.2 (d); 43:21-7(a)(1)

that such a relationship, that is hemmed in and defined at every level by federal and state law, is a voluntary contract, that merely creates a debt, makes a mockery of the"involuntariness" requirement under *Anderson-Feiring*, in addition to grossly misinterpreting State law. As the dissent correctly pointed out, far from being afforded a benefit, non-profit employers are burdened with a new duty to "support the [UC] fund" in order "to benefit the former employees and the public good, not the employer. App. 28, 29.

The State's statutory scheme leaves no doubt that contributions and reimbursements are simply two alternative means of funding the UC trust fund, with these payments methods being no different, substantively and functionally. The reimbursements are not, as the Third Circuit stated, an alternative to the imposition of liability for a tax, they are simply an alternative way of satisfying that liability. Indeed, in two cases in which this Court construed the liability of certain non-profit entities under the FUTA amendments, it repeatedly described the alternative payment rights accorded to the employers as "taxes," and never even hinted that their status as taxes would depend on which form of compliance the employer elected. *See*, *St. Martin Evangelical*, *supra*, 451 U.S. at 775-777; *Grace Brethern Church*, *supra*, 457 U.S. at 396-98, 411-417.

In sum, prior to the *Suburban II* decision, and its refusal to apply this Court's test without the addition of a host of other factors and policy considerations to limit the granting of tax status, it is unlikely that the Third Circuit would have felt compelled to search, as it did, for reasons to avoid the obvious conclusion that these payments are excise taxes. The majority's conclusion in this case has nullified the State's ability to tax non-profit employers with respect to the individuals in their employ, even though such taxes are expressly permitted by the FUTA. Its decision has defeated the State's statutory intent and purpose of taxing non-profit employers, which the State regards as participants who must bear the costs of funding and

maintaining the UC Fund. The Third Circuit's decision must therefore be reversed.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

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